

IT 97-15

Tax Type: INCOME TAX

Issue: Penalty Under 1002(d) - Failure To File/Pay Withholding

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
ADMINISTRATIVE HEARINGS DIVISION
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE)	
OF THE STATE OF ILLINOIS,)	
Petitioner)	No.
)	
v.)	SSN:
)	
TAXPAYER,)	
as responsible officer)	Linda K. Cliffler,
of CORPORATION Inc.)	Admin. Law Judge
)	

RECOMMENDATION FOR DISPOSITION

APPEARANCES: William E. Borenstein for TAXPAYER; Shepard Smith, Special Assistant Attorney General, for the Illinois Department of Revenue.

SYNOPSIS:

This matter comes on for hearing pursuant to the protest of the Notice of Deficiency ("NOD") Number XXXX issued by the Department against TAXPAYER on October 13, 1994, as responsible party of CORPORATION, Inc. (hereinafter referred to as "CORPORATION"). The NOD represents the officer's liability for withholding taxes admitted by CORPORATION as due to the Department for the third and fourth quarters of 1990 and the first, second and third quarters of 1991, but which are unpaid.

A hearing in this matter was held on June 10, 1997. Following the submission of all evidence and a review of the record, it is recommended that this matter be resolved in favor of TAXPAYER.

FINDINGS OF FACT:

1. TAXPAYER was not an officer or director of CORPORATION, Inc. (Tr. pp. 14-15, 73)
2. TAXPAYER was the president of Co., Inc. (hereinafter "COMPANY") (Tr. pp. 14, 73; Dept. Group Ex. 4, pp. 19-22)
3. Taxpayer's mother TAXPAYER'S MOTHER was the president of CORPORATION and signed the IL-941's. (Tr. pp. 16-17; Dept. Group Ex. 4, pp. 12-18)
4. No corporate checks were signed by taxpayer. (By stipulation of parties, Tr. p. 5)
5. TAXPAYER executed a sworn affidavit dated November 22, 1995 in which he states he is the Chief Operating Officer of CORPORATION and responsible for its financial affairs. (Dept. Group Ex. No. 4, p. 24, Tr. p. 12)
6. The Notice of Deficiency was issued against taxpayer on October 13, 1994. (Dept. Ex. No. 1)
7. The Department's Revenue Tax Specialist, Louise Diefenback, who issued the Notice of Deficiency, based her determination that taxpayer was a responsible party of CORPORATION on the field auditor's notes, which she understands stated that taxpayer was the president of COMPANY, which controlled CORPORATION, and that he would try to obtain a loan to pay the taxes. She did not verify that he was an employee or director of CORPORATION. She examined the tax returns which were filed by CORPORATION and determined that they were signed by J. B. Schreiber. She did not examine any cancelled checks. (Tr. pp. 14-16)

CONCLUSIONS OF LAW:

The penalty at issue herein is based upon the withholding tax liability of CORPORATION for the third and fourth quarters of 1990 and the first, second and third quarters of 1991. The corporation submitted to the Department the required tax returns without payment for the amounts stated therein. The Department seeks

to impose personal liability on TAXPAYER pursuant to Ill. Rev. Stat. 1991, ch. 120, ¶1002(d),¹ which provides:

Any person required to collect, truthfully account for, and pay over the tax imposed by this Act who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over...For purposes of this subsection, the term "person" includes an individual, corporation or partnership, or an officer or employee of any corporation (including a dissolved corporation), or a member or employee of any partnership, who as such officer, employee or member is under a duty to perform the act in respect of which the violation occurs.

The Department of Revenue issued a Notice of Deficiency against the taxpayer on October 13, 1994. According to the testimony of Revenue Tax Specialist Louise Diefenback, the basis for the determination that taxpayer was a responsible officer of CORPORATION was the field auditor's notes, which were not offered into evidence. She stated that the notes indicated that COMPANY controlled CORPORATION, and that TAXPAYER was president of COMPANY, and that he had offered to attempt to secure a loan to pay the taxes.

At the time the NOD was issued, there was no evidence that TAXPAYER had any connection with CORPORATION. He was not an employee, an officer, or director. The Department had no checks of CORPORATION which he had signed. The IL-941's were signed by TAXPAYER OR TAXPAYER'S MOTHER, but on examination, the revenue tax specialist agreed that they appeared to be signed by taxpayer's mother, TAXPAYER'S MOTHER. Prior to the issuance of the NOD, the Department had other IL-941's in its possession which she signed using her full name and which exhibited the same handwriting. Inasmuch as TAXPAYER'S MOTHER was the president of CORPORATION and all the tax returns were apparently signed by the same

¹ The liability for payroll taxes herein accrued in 1990 and 1991. Therefore, the statute which applies is Ill. Rev. Stat. 1991, ch. 120, ¶1002(d). The Uniform Penalty and Interest Act, 35 ILCS 735/3-7, which provides for a personal liability penalty, is effective for taxes incurred January 1, 1994 and later.

individual, it was not reasonable to believe that the returns were signed by anyone other than TAXPAYER'S MOTHER.

In a letter dated September 6, 1994 to Louise Diefenback (Dept. Group Ex. 4, p. 20), which was written prior to the issuance of the NOD, TAXPAYER stated that COMPANY, as the majority shareholder of CORPORATION, was making payments on behalf of CORPORATION, and that Jackie Spacone of the Department of Revenue had handled the accounts. This letter, read in conjunction with the field auditor's notes, should have raised the question whether TAXPAYER was seeking a loan in his capacity as president of COMPANY or personally.

Under Section 904 of the Illinois Income Tax Act, the NOD is deemed to be *prima facie* correct and *prima facie* evidence of the correctness of the tax shown to be due. At the time the NOD was issued, however, Ms. Diefenback had absolutely no information that TAXPAYER was an officer, director, or employee or any responsible party for CORPORATION. The Department had insufficient evidence prior to issuing the NOD to meet the minimum standard of reasonableness. Mitchell v. Department of Revenue, 230 Ill. App. 3d 795 (1st Dist. 1992); Masini v. Department of Revenue, 60 Ill. App. 3d 11 (1st Dist. 1978) (the method employed by the Department in correcting a taxpayer's return must meet some minimum standard of reasonableness). Therefore, the element of minimum reasonableness which is subsumed into the *prima facie* correctness of the NOD has been successfully challenged by the taxpayer.

WHEREFORE, for the reasons stated above, it is my recommendation that the Notice of Deficiency against TAXPAYER be cancelled.

Date:

Linda K. Cliffel
Administrative Law Judge